VZCZCXYZ0002
RR RUEHWEB

DE RUEHLP #0023/01 0261807
ZNY CCCCC ZZH
R 261807Z JAN 10
FM AMEMBASSY LA PAZ
TO RUEHC/SECSTATE WASHDC 0513
INFO RHEFDIA/DIA WASHINGTON DC
RHEHAAA/NATIONAL SECURITY COUNCIL WASHINGTON DC
RUCPDOC/USDOC WASHINGTON DC
RUEAIIA/CIA WASHINGTON DC
RUEHAC/AMEMBASSY ASUNCION
RUEHBO/AMEMBASSY BOGOTA
RUEHBR/AMEMBASSY BRASILIA
RUEHBU/AMEMBASSY BUENOS AIRES
RUEHCV/AMEMBASSY CARACAS
RUEHLP/AMEMBASSY LA PAZ
RUEHME/AMEMBASSY MEXICO
RUEHMN/AMEMBASSY MONTEVIDEO
RUEHPE/AMEMBASSY LIMA
RUEHQT/AMEMBASSY QUITO
RUEHSG/AMEMBASSY SANTIAGO
RUEHSO/AMCONSUL SAO PAULO
RUEHUB/USINT HAVANA 0050
RUEKJCS/SECDEF WASHINGTON DC

C O N F I D E N T I A L LA PAZ 000023

SENSITIVE
SIPDIS

E.O. 12958: DECL: 2019/12/16
TAGS: ECON PREL BL EINV EFIN SNAR ETRD
SUBJECT: Morales begins next administration in strong economic position

REF: 09 LA PAZ 1417

CLASSIFIED BY: JohnSCreamer, ChargeD'Affaires; REASON: 1.4(B), (D)

¶1. (U) SUMMARY. As President Morales is inaugurated into his second term in office, Bolivia enters 2010 with strong economic fundamentals. Although concerns remain about the investment climate, GDP continues its strong growth (6.1% in 2008, 3.25% in 2009), inflation fell significantly (from 11.8% in 2008 to 0.25% in 2009), reserves are high, the exchange rate is stable, and the financial system is strong. With Morales likely to continue with similar economic policies, a recent briefing from the World Bank shows that the Bolivian economy appears to be in good shape for ¶2010. END SUMMARY.

¶2. (U) Bolivia has been relatively isolated from the global economic crisis, posting GDP growth rates above those in the region. With an average growth rate of 3.4% from 1996-2005 and an average of 5.2% in 2006-2008, growth peaked at 6.1% in 2008. Growth slowed in 2009, but GDP still managed to grow at 3.25% and is expected between 3-4% for 2010. The main factors in recent GDP growth have been the mining sector, public investment, the transportation sector, and continued high remittances.

¶3. (SBU) 2010 growth will likely be more dependent on public investment as foreign and private investment continues to decline. The GOB has the funds for public sector investment but managerial capacity and technical skill will be a major constraint. The Morales government has plans for large infrastructure projects, some of which will be managed by the state run oil company YPFB. An expected general rise in commodity, mining, and gas prices will also have a positive effect on GDP.

¶4. (U) Bolivian Central Bank policies have been praised by the World Bank and IMF in bringing down inflation, maintaining a stable

exchange rate, and increasing international reserves. Lower food prices and reduced domestic demand contributed to the lowering of the inflation rate from 11.8% in 2008 to 0.25% in 2009. It is expected to remain low for 2010, with the IMF expecting something closer to 4%.

¶5. (U) The exchange rate has been set at a crawling peg and the current rate of 7.07 Bolivianos = US$1, which the World Bank believes reflects market equilibrium and does not anticipate pressure to devalue in 2010. Reserves rose from $3.2 billion in 2006 to $8.6 billion in 2009, and will likely continue to grow throughout 2010. Still, with large public infrastructure projects planned, and with the GOB need to continue financing social programs like the popular conditional cash transfers called "bonos," there is no guarantee they will not be tapped as a funding source.

¶6. (U) The financial system also continues to remain strong. Interest rates remain low at 8.3 %, and bank deposits have steadily grown over the last 18 months. Additionally, the percentage of deposits held in dollars has dropped from 95% in 2005 to closer to 60% today, a sign of increased confidence in the financial system. Still, the banks' accumulation of excess reserves due to weak demand for loans is disturbing. Private sector investment fell from 18% of GDP in 1998 to only 7% in 2009. This poses a medium-term threat to continued growth.

¶7. (U) Morales has chosen to keep Minister of Economy and Finance Luis Arce in place for the time being. This signals that he approves of his work and that things will continue along the same path. Arce is generally seen by economists, international rating agencies, business people, and the international financial institutions as competent, despite Morales' socialist rhetoric. In his inauguration speech, Morales praised Arce for his care of the economy and for taking the country through the world economic crisis with impressive GDP growth, an historic increase in exports and reserves, and keeping inflation low.

¶8. (U) The IMF concluded an Article IV Consultation with Bolivia on January 21 and the overall assessment is a positive one, highlighting the positives mentioned above and offering minor suggestions for improvements in the tax structure and investment climate. The World Bank also recently told us that they expect the economic fundamentals to stay strong through 2010. Rating agencies Moody's and Fitch both upgraded Bolivia in September 2009 (from B3 to B2 and from B- to B respectively), citing strong fiscal policy and decreased political unrest.

¶9. (U) The Morales government has utilized three conditional cash transfer programs (bonos) to assist needy groups in the population: public school children, mothers with young children, and retirees (ref A). The GOB claims a 10 point fall in extreme poverty for the period 2007-2008 as a result of the bono programs. The World Bank is skeptical of these figures, but it agrees the programs are positively affecting poverty rates. World Bank figures show about a 1% decrease in extreme poverty and a decrease of 3% in overall poverty rates since 2005, but is currently revising this data.

¶10. (C) World Bank economists also told us that they estimate around $500-600 million (or 3% of GDP) enters the economy from narcotics profits. They note that some estimates range up to $1 billion, but there is little proof of such. The World Bank believes that recent economic growth can be accounted for through mining, hydrocarbons, and the informal economy. The World Bank does not see evidence of an exorbitant amount of drug money floating through the banking system and believes that the majority of profits from processing and exporting the coca go to foreign cartels who control

the process. The money that stays in Bolivia is mostly due to the sale of the coca leaf and little of the added value remains here. Still, they agreed that it is important to continue to monitor the issue.

¶11. (SBU) COMMENT. With the stage set for a relatively stable economic situation in Bolivia in 2010, Morales will have more leeway to continue with his economic policies. Having already nationalized gas transport and telecommunications, he will likely continue with his announced plans of nationalizing the electric sector and possibly the railways, focusing on those companies that were partially privatized under previous governments. The large reserves provide a cushion to finance such actions if needed. He will also continue with social programs to help needy portions of the population. It will likely be 3-4 years before the effects of the slowdown in international investment will show up in the economic data. END COMMENT.
Creamer